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To: The Newark Municipal Council

RE: 2004 Management and Financial Plan

Like a good mason, our City has continued to labor at a steady pace, putting the bricks in place that will make Newark strong for the long haul.

Our bricks are projects like the new Home Depot, bringing modern retailing to our Central Ward. They are the reuse of wonderful buildings like Hahne's and the Griffith building to bring market rate housing to the heart of Downtown. They are the new houses springing up in every ward, expanding the base of homeowners within our city and bringing new retail and commercial facilities that provide jobs for our citizens.

And they are the public projects as well, from the new schools for our children throughout the City and the deepening of our seaport, to the reopening of the Passaic River waterfront and the return of the trolley to our streets. Brick by brick, we are building a new Newark.

In 2004, we will lay even more bricks. McCarter Highway will be smoother and wider. More housing will be built, both Downtown on a new Mulberry Street and throughout the wards. More new schools will get underway. The first new firehouse in over three decades will be put into service. And, yes, work will start on a new major league arena.

Just as a good wall needs a solid foundation, our bricks require a solid financial foundation and the 2004 budget provides that stable base. There are no shocks or surprises in this budget, just the kind of solid management decisions that are necessary to maintain our fiscal health and allow the progress to continue.

That solid management is reflected in departmental operations, where we have used attrition to trim our workforce by 169 positions, while bringing better technologies into use that will allow us to provide the same services with the reduced staffing levels. It is reflected in our revenue expectations, where we will be focusing on increased enforcement to improve collection rates in special taxes and utility billings, and to maintain improved revenue levels in our municipal courts. And it is reflected in our continuing success at bringing new private investment to the City.

Perhaps most importantly, that solid management is reflected in the long-term approach that we continue to take regarding our financial plans. Our perspective is not just on the current year's requirements, but rather on the needs of the City over the next several years. Our goal is to follow a path that will provide stability to our tax rate, dependability in our service delivery and predictability for those who live, work or seek to invest in Newark.

At the heart of our strategy is the objective of restoring structural balance to the City budget. By "structural balance," I mean a situation in which the recurring revenues that the City can expect are equal to the recurring costs of running the City. Structural balance means that services can be maintained without the need to dramatically increase tax rates year after year.

Newark does not now enjoy such balance. If no action is taken, our City will face budget gaps that start at $40 million for 2004 and grow by about $20 million per year thereafter. But we are taking action, and this budget represents the first year in a five-year plan to achieve and maintain that structural balance.

Our plan consists of four main components.

1. Control of municipal spending;
2. Maximizing collection of current revenues;
3. Expansion of the tax base; and
4. Temporary use of Port Authority lease payments to smooth the transition.

Control Of Municipal Spending

The 169 positions that we are eliminating in this budget may be the most obvious step in our efforts to control costs, but it is far from the only step. My administration is at the forefront in using technology to improve the efficiency of municipal operations, and in the next few years, we will dramatically expand that use. Our Web-based systems will include hand-scanning techniques to track City employees attendance; electronic data collection and reporting by all City inspectors; an electronic, City-wide work order system to monitor every task, and direct electronic collection of taxes, utility bills, license fees and other City revenues.

We also will seek economies in other ways. This year, we will introduce our employees to managed health care, as we work to get spiraling health insurance costs under control. We will continue to press for the transfer of welfare operations and jail operations to the County of Essex, as is the case in most of the State's major cities. And we will continue to look for opportunities to achieve savings through contracting out inefficient municipal services.

Maximizing Collection Of Current Revenues

The second leg of our strategy involves improving the collection of revenues already owed to the City. While we do a good job of collecting our property taxes and have made real progress in collecting traffic fines, we need to become equally adept in collecting the other revenues that are due us. For 2004, our initial targets will include those special taxes that we collect on payroll, parking and hotels. By instituting a system of monitoring and enforcement, we will make sure that everyone pays their fair share of the costs of running the City. A similar effort at enforcement will also be put in place regarding our tax-abated properties.

Expansion Of The Tax Base

The third piece of our plan is that of expanding our tax base. This will be accomplished in two ways: By continuing to encourage new private investment projects within the City, and by seeking the authority for a new tool to free up still more land for productive use.

As to new projects, I am excited about the prospects for further investment in our City. With four major residential projects announced for our Downtown, the likelihood that the deepened channels at the seaport will attract more business and with national companies finally rediscovering Newark, I am hopeful that we can grow our ratable base by 5% per year or more.

To try to speed that growth, I will be asking the State Legislature to grant Newark the power to levy a tax on the storage of shipping containers. While I understand the need to support operations within the port district, the quantity of containers now littering the Newark landscape has soared out of control, tying up hundreds of acres of valuable industrial land. By applying an appropriate tax, the City will either gain a reasonable revenue from tolerating these eyesores, or preferably will regain the availability of that land for positive, job-creating development.

Before I turn to the final element of our plan, let me say a few more words about our ratable base. A year ago much of the talk around the budget centered on the revaluation of property, which was done for the first time in over 40 years. One year later, I think it is fair to say that the revaluation has been proven to have been done fairly and accurately.

I say that based on the evidence that has emerged both from the courtroom and from the marketplace. In the courts, the vast majority of appeals brought regarding the revaluation have been decided in favor of the City, testimony to the equity of the assessment process. In the marketplace, sales of property have continued at a healthy pace, with prices generally reflecting the values shown by the revaluation.

I say this not by way of defense of the revaluation process, although I will commend Evelyn Laccitiello, our Tax Assessor, for an outstanding job in managing an extremely

difficult process. Instead, I say this to illustrate that the results of the revaluation are an accurate reflection of the progress we have made in our City. The revaluation indicated that property values in Newark rose by 96% between 1998 and 2003. With the revaluation results now validated, I can say again that this real-and dramatic-increase in the value of real estate in Newark is clear evidence that our progress is genuine.

Over the next five years, I expect the steps I have outlined above will gradually close the budget gaps that I spoke of earlier, and that the City will achieve true structural balance. I do not expect that such progress will occur overnight.

Temporary Use Of Port Authority Lease Payments To Smooth The Transition

Fortunately, our negotiations with the Port Authority of New York and New Jersey afford us the opportunity to reach that goal without financial disruption along the way. Because our settlement with the Port Authority regarding Newark Liberty International Airport and our seaport provided for Newark to be treated on a parity with New York City, the recent agreements on the east side of the river have triggered a requirement that will provide more revenue to Newark. We have asked that the payment of those additional funds be structured to be spread over time, so that they can be used to bridge the gap from our present status to one in which we can meet our future financial goals.

We do not expect to use all of the additional funds in support of the operating budget. To the extent that the funds exceed the amount needed to stabilize the budget, we will pledge those funds to programs that are investments in the development of our community. If, as I expect, we are successful in accelerating the pace of our financial progress, all of the Port Authority funds that are made available will also be used to encourage development.

The net result of this plan is that we will be able to keep the true tax rate low in real terms. As I indicated a year ago, the 2003 true tax rate for Newark, the rate determined by dividing the amount of tax by the market value of a property, was the lowest of any major urban area in the state and lower than the average for all municipalities in both Essex County and the state. For 2004, this budget projects a nominal tax rate that will increase by about 5%, to $2.26. The 2004 Management and Financial Plan proposes a total appropriation of $627,676,107.00. Of this total $491,709,143.00 is appropriated for Municipal Purposes; $85,864,815.00 is appropriated for School; and $50,102,149.00 is appropriated for County. As a result, I fully expect that for 2004, the true tax rate for Newark will remain the lowest of any major urban area in New Jersey and low by comparison to most towns in the state.

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While I have provided a broad outline of how we have reached that tax rate, it is interesting to understand the details that lead to that result. The following highlights the key data about this year's budget.

Departmental Appropriations

Despite paying for negotiated salary increases and incremental advances to virtually all employees, we have been able to keep the cost of running the City departments to an increase of 2.5%. This has been possible in significant part due to the cuts in positions discussed previously, which saved about $7 million. No significant changes in municipal service are expected.

Mandatory Appropriations

Costs of most of the mandatory items are stable or declining this year, which helps keep taxes under control. Deferred charges are down by 18%, due to a reduction in bills carried over from prior years. School debt service is also reduced, going down by 15%, as some other bonds have been retired.

County and School Appropriations

Since neither the County nor the School tax requirements are final at this time, they have been estimated to increase by 3%, based on recent trends.

Revenue

The City's revenue picture is the major reason for the projected budget gaps over the next several years. In general, the revenues exhibit little growth and remain essentially flat from year to year.

A significant contributor to this problem has been the policies followed by the State of New Jersey. For several years, the revenues distributed to municipalities have remained capped, despite the constant pressure of rising costs and despite the fact that many of the revenues collected by the State as the source of those distributions grew annually. The 2004 budget does not contemplate any change in this picture, with the same $111 million to be received from State sources.

Most of the local revenues are similarly flat, typically because they are levied at a fixed rate that does not grow with inflation. Notable exceptions to that are the special taxes charged on payroll, parking and hotels, which are collectively expected to contribute about $3 million, or 6.5% in additional revenue.

The budget suffers from the loss of some one-time revenues, including $8.2 million generated from the refunding of the City's pension obligations and $1 million from capital surpluses. The City's balance sheet remains strong, with a surplus of $11 million expected to be available to support the budget.

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Water and Sewer Utility

In addition to setting out our plans for the general government, the annual budget also outlines the steps that we will take in managing our Water and Sewer Utility. For nearly a decade the City has been able to provide our citizens with quality services from our Water and Sewer Utility without requiring an increase in the rates charged for those services. We have reduced the workforce through attrition, improved collection of delinquent accounts and found other savings in order to make such rate stabilization possible.

While we have kept our costs down, the costs we pay to other agencies for water and sewer services have risen dramatically. In 2003 alone, annual costs for the Passaic Valley Sewage Commission (PVSC) climbed by $5.2 million. Annual costs for the North Jersey District Water Supply Commission soared by $3.7 million, and costs for the Joint Meeting sewer authority jumped by $1 million.

Under New Jersey law, our Utility must have a balanced budget for each year, with the full cost of services offset by the amount of fees collected, plus any surplus that may be available. For the past several years, fee revenue has not been sufficient to meet expenses, but the budget has remained balanced through the availability of surplus funds. That surplus is now exhausted, and will not be available for future budgets.

An additional problem is that of consumption. Largely due to conservation measures imposed during the drought of 2002, consumption of water is down by about 5%.

The combination of these factors, higher mandated costs, an exhausted surplus and lower consumption, adds up to a budget that will not meet the legal requirement to be balanced, either for 2004 or the foreseeable future. The lack of balance has two major, negative implications:

1. The full amount of any deficit must be made up by an appropriation in the next year's regular City budget. This means that property taxes will be raised to pay water and sewer costs.

2. All of the debt owed by the Utility will be treated as the City's debt. This will dramatically reduce the City's capacity to borrow for other purposes and may result in higher interest rates for City borrowing.

In order to avoid these problems, this budget projects that the current rates for both water use and sewer services be increased. Our proposal would change the water rate from $13.43 per 1000 cubic feet to $15.31 per 1000 cubic feet, an increase of 14%. Sewer rates would go from $14.40 per 1000 cubic feet to $17.14 per 1000 cubic feet, an increase of 19%.

To put the new rates in perspective, after the increase, Newark's water rate will be the second lowest in Essex County, with only Essex Fells having lower rates. Newark's new rate will also be more than 30% lower than the current rates in Jersey City and Elizabeth.

Since the costs of the Utility cannot be reduced any further without serious consequences to service, the choice is not whether or not to raise rates, but whether to raise rates or to raise property taxes. From our perspective, using property taxes to balance the Utility budget is inherently unfair, since it means that those who use the water are not the same as those who pay for its use. In addition, using taxes to solve the problem means that all of those who are exempt from taxation, including the County and State government, the major colleges and universities and the non-profit and church organizations, will not be required to pay for their fair share of the water and sewer bill.

By comparison, if the budget is balanced through the use of higher rates, the full cost will be borne by those who actually use the water and the sewer system. The cost will be spread across all users, including all of those who are exempt from paying property taxes. With so much of the City in exempt status, this difference means that the average homeowner will pay less if the increase is done through rates than if the increase is done through taxes.

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In light of the limitations imposed by our revenue picture, I am satisfied that the plan that I am hereby submitting represents a significant accomplishment that will provide the stability in taxes, dependability in services and predictability for investment that are necessary for our continued progress. This 2004 proposed Municipal Budget will provide the firm foundation we need to make sure that our wall will be built strong and straight.

Sincerely yours,

Sharpe James
Mayor